INVESTING IN ASIA

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Rahul Chadha

Rahul Chadha, Co-Chief Investment Officer of Mirae Asset Global Investments (Hong Kong), notes that China's market may wobble but the demographic, aspirational and structural trends across Asia are as strong as ever

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Asia's Long-Term Prospects Remain Bright

What gives Mirae Asset the edge when it comes to investing in Asia equities?

You need a strong on-the-ground presence if you want to be a strong bottom-up stock picker in Asia. We have teams in Hong Kong, India, China, Korea and Taiwan who identify trends early. We seek established or emerging sector leaders at the right price.

All our potential investments are rated by a "Competitive Scorecard", which is Mirae Asset's proprietary measure of shifting market dynamics, a company's track record and sustainability of returns. Stocks must be top quartile performers to make it through to selection. Analysis is deliberately tight and stock-specific.

Macro is just noise 80% of the time. Only when there is a step-change do we take top-down economic factors into approach. In recent years, currency movements, the downgrades of Indonesia's prospects and India's changing monetary policy were all chances to buy good companies cheaply. But the majority of the time, we are company-specific.

You focus heavily on the power of the Asia consumer. How robust is that theme at the moment?

Our Sector Leader funds and Great Consumer funds focus heavily on the rise of the Asian consumer, a long-term structural trend. Fast-growing middle classes are heading for the point of self-actualisation when spending changes from "I need" to "I want". 400 million Chinese consumers have reached the US$8,000 annual income threshold that makes tourism and other discretionary spending a reality.[1] Asian consumers prefer their local brands. Brands are responsive too. They are early to spot trends, develop them and move into new territories.

We continue to stay constructive on Asian equities despite recent market volatilities. Given low inflation and generally high real interest rate in the region, we expect to see more monetary easing in the coming twelve months, particularly in China and India. In addition, Asia being a large commodity consumer is a beneficiary of weak commodity prices, and we expect to see this positive catalyst play out in coming quarters as consumer demand rebounds. Lower raw material prices are already leading to margin expansion across a number of sectors and markets.

[1] CLSA, Mirae Asset Global Investments (2015)

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Should your investors worry about China?

Amidst the highly emotion-led market conditions in China, we believe prices often move far from economic and company fundamentals. As such, we maintain our strategy to stay grounded and focus only on high quality companies. We took advantage of the market volatility and added exposure in Chinese telecom and insurance names that were trading at attractive valuations. As a testament to our strategy of focusing on quality, stock selection in China was among the key contributors to the fund's outperformance in recent months.

Where next for China?

We can expect more volatility in the months ahead. We had in the past voiced concerns about the frothy valuations in the A share market, up nearly 100% since November 2014 in a slowing economy.[2] The government's strategy of using household assets to repair corporate balance sheets through a "stock market feel good" approach was always fraught with risks. Near term, volatility would be huge because of the inability of retail investors to liquidate expensive small-cap thematic stocks listed in Shanghai & Shenzhen. Unfortunately, the Chinese authorities' intervention and efforts to stabilize the stock market are moves away from a market- based economy and a serious dose of reforms is required in coming months to undo the damage. Even so, China has shown determination when it comes to other areas of reform, so the outlook over the longer term is positive. We remain constructive on a multi-year view and very much focused on resilient, quality businesses.

What about India?

We believe India is most attractive equity market in the medium term – and it has a low exposure to China. It continues to feature heavily in our regional portfolio too. We are seeing growth recovery in India, albeit it has been slow. On the ground, we are gaining more confidence in the efforts by the Modi government, such as institutionalising various government ministries. We are also seeing encouraging developments at state level as they compete for investment. The announcement of a US$5 billion Foxconn in Maharashtra is a recent example.[3]

[2] Wind Financial Terminal, Mirae Asset Global Investments (June 2015)

[3] "Foxconn Plans to Spend $5 Billion on Factories in India's Maharashtra State," The Wall Street Journal (August 2015)

But can India really deliver, given the woeful state of its infrastructure?

The Modi government continues to face plenty of challenges: defense, railways and roads spends have picked up, however lots needed to done to restore the health of state electricity boards. On the policy front, the monsoon parliament session has seen two weeks of deadlock, with important legislation such as a national goods and services tax on the agenda. Meanwhile, the government has announced a comprehensive package worth Rs 700bn(US$11bn) to recapitalize the public banks over the next four years.[4]

Are Indian equities fully priced?

Near term, the market remains vulnerable to pullback on the back of high valuations in consumer staple and mid-cap companies as growth recovery in rural economy remains muted. Even so, India was the best performing market in the Asia ex-Japan region in July and was the only market in positive territory. As India is a heavy importer of fuel, lower global crude oil prices were a key factor supporting for the market.

What about the macro and business fundamentals?

Macroeconomic data has been soft. Industrial production growth moderated to 3.2% year-on-year in June, from 3.3% in March.[5] The latest quarterly earnings season was a mixed bag. Consumer and autos have beaten expectations on back of strong margin expansion led by lower raw material costs, while commodities and state-owned banks have disappointed.

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[4] Modi Takes Aim at India's Ailing Public Banks," Financial Times (August 2015)

[5] Goldman Sachs Portfolio Strategy Research, Mirae Asset Global Investments (2015)

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What is the outlook for the rest of the Asia region?

We expect a slower growth scenario in China but there has been no change to our portfolio positioning. We are cautious on Korea and Taiwan as they are most exposed to global trade, but we retain our positions focused on regional consumption and tourism.

Across the region, the benefits of central bank easing should come through in the second half of the year. And the weakening of commodity prices is a net positive for almost every Asian economy as all are heavy importers of fuel and raw materials.

Any rise in US rates may have a negative impact on the ASEAN region, but the region as a whole is far less vulnerable that it was during the Asian Financial Crisis or the more recent taper tantrum of 2013.

Philippines is the bright spot in the ASEAN region, with GDP growth of around 6%, strong demographics, a domestic-led economy and a current account surplus.[6]

On the very long-term view, the demographic advantage is very much in place. The average age is just 27 in India, 36 in China and 23 in the Philippines.[7] Economies have low leverage when compared to their developed market peers and political structures are largely stable across the region. China's growth trajectory will be a slow grind, hence our overall neutral stance, with an emphasis on consumption, internet, telecom, healthcare and the like.

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[6] Goldman Sachs Economics Research, Mirae Asset Global Investments (2015)

[7] UN, Department of Social Economic and Social Affairs, World Population Prospects (2012 Revision), Mirae Asset Global Investments (June 2015)

Global Offices

Mirae Asset Global Investments
East Tower 26F, Mirae Asset CENTER1 Bldg,
67, Suha-dong, Jung-gu,
Seoul, Korea (100-210)
Tel.+82-2-3774-8200

Mirae Asset Global Investments (HK)
Level 15, Three Pacific Place, 1 Queen's
Road East, Hong Kong, HK
Tel.+852-2295-1500

Mirae Asset Global Investments (UK)
4-6 Royal Exchange Buildings,
London, EC3V 3NL, United Kingdom
Tel. +44-20-7715-9900

Mirae Asset Global Investments (USA)
1350 Avenue of the Americas,
33rd Floor, New York, NY, 10019, USA
Tel. +1-212-205-8300

Mirae Asset Global Investments (Taiwan)
6F, NO. 42, Sec.2 Zhongshan N. Rd.,
Taipei City 10445, Taiwan (R.O.C)
Tel. +886-2-7725-7555

Mirae Asset Global Investments (India)
Unit No. 606, 6th Floor, Windsor Building
Off. C.S.T Road, Vidyanagari Marg.
Kalina, Sanatacruz (East), Mumbai 400 098, India
Tel. +91-22-6780-0300

Mirae Asset Global Investments (Brazil)
Rua Olimpíadas, 194/200,
12 Andar, CJ 121, Vila Olímpia
São Paulo, CEP 04551-000, Brazil
Tel: +55-11-2608-8500

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